LEGISLATIVE SERVICES AGENCY
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FISCAL IMPACT STATEMENT

LS 6510 | **NOTE PREPARED:** Dec 20, 2007
BILL NUMBER: SB 170 | **BILL AMENDED:**

SUBJECT: Community investment tax credits.

FIRST AUTHOR: Sen. Dillon | **BILL STATUS:** As Introduced
FIRST SPONSOR:

FUNDS AFFECTED: X GENERAL | **IMPACT:** State
X DEDICATED
FEDERAL

Summary of Legislation: This bill establishes a community investment tax credit against state tax liability for investments that: (1) qualify for a federal new markets tax credit against federal income tax liability; and (2) are made by a certified development entity that agrees: (A) to dedicate 100% of the certified development entity's investments for which the certified development entity may receive a federal new markets tax credit for reinvestment in low income communities in Indiana; (B) to invest at least 80% of the certified development entity's total assets in low income community businesses in Indiana; and ©) to continue to reinvest at least 30% of the last state certified investment in eligible businesses for a period of at least 14 years after the last credit allowance date for the certified development entity's last state certified investment.

Effective Date: January 1, 2008 (retroactive).

Explanation of State Expenditures: *Department of State Revenue (DOR):* The DOR will incur additional expenses to revise tax forms, instructions, and computer programs to reflect the new Community Investment Tax Credit. The Department's current level of resources should be sufficient to implement this change.

Indiana Economic Development Corporation (IEDC): The bill requires the IEDC to establish a program for accepting and reviewing applications for and certifying Community Investment Tax Credits. In addition, the bill requires certified development entities to annually report to the IEDC on their programs. The report must include: (1) information on number and amount of state certified investments and federally qualified equity investments made by the entity in Indiana; (2) a description of each eligible business receiving an investment attributable to a state certified investment; (3) an update on the financial status of each eligible business; (4) an update on new jobs, increased wages, total investment, and revenue impact derived from the state certified investment; and (5) the sum of the state credits designated by the certified development entity. The bill requires this report to be submitted to the Executive Director of the Legislative Services Agency. Should the IEDC certify a federally qualified equity investment as a state certified investment, the bill requires that a certification letter be given to the applicant.

The IEDC's current level of resources should be sufficient to fulfill these administrative tasks.

Explanation of State Revenues: *Summary:* This bill establishes the Community Investment Tax Credit allowing development entities certified by the IEDC to receive tax credits for equity investment that qualifies for the federal New Markets Tax Credit (NMTC) and is approved by the IEDC. The credit may be taken against the taxpayer's Adjusted Gross Income (AGI) Tax liability, Financial Institutions Tax liability, or Insurance Premiums Tax liability. The amount of credits that could potentially be claimed each year is indeterminable and depends on development entities qualifying for the federal NMTC and being certified for state tax liability credits by the IEDC. The credit applies only to qualified equity investment made after December 31, 2007, and can only be claimed beginning in tax year 2008. As a result of these circumstances, any fiscal impact from the credits likely would not arise before FY 2009.

Background Information: Investment Tax Credit: The nonrefundable tax credit is equal to 5% of the equity investment held by a corporate or individual taxpayer, including a pass through entity, that is certified for the credit by the IEDC. The only equity investment that qualifies for the state credit is an equity investment that qualifies for the federal NMTC. The bill requires the IEDC to establish a program to certify community investment entities that are qualified to receive the federal NMTC as state certified development entities. The bill requires the IEDC to certify a federally qualified community investment entity as a state certified development entity if the entity:

(1) is qualified to receive the federal NMTC;

(2) has a record of successfully providing capital or other financing to eligible businesses located in Indiana;

(3) has a record of successfully reinvesting equity investments qualified for the federal NMTC in Indiana;

(4) commits in an agreement with the IEDC to allocate 100% of its allocation of federal NMTCs for reinvestment in low-income communities in Indiana;

(5) commits in an agreement with the IEDC to continue to loan to or otherwise reinvest in eligible businesses in Indiana for at least 14 years after the last federal NMTC allowance date for the entity's last state certified investment at least 30% of the applicant's state certified investment; and

(6) commits in an agreement with the IEDC to invest at least 80% of its aggregate gross assets (including reserves) in eligible businesses.

The tax credit is nonrefundable, and unused credit amounts may not be carried back. However, a taxpayer may carry forward any unused credit amount for up to three subsequent taxable years. For pass through entities, the credit may be claimed by shareholders, partners, or members in proportion to their distributive income from the pass through entity. The bill provides that in the event federal NMTCs are disallowed or recaptured by the IRS, the state credits for the same equity investment are terminated only to the extent the state credits are disallowed or recaptured by the IEDC.

Revenue from the AGI Tax on corporations, the Financial Institutions Tax, and the Insurance Premiums Tax is distributed to the state General Fund. Eighty-six percent of the revenue from the AGI Tax on individuals is deposited in the state General Fund, and 14% of the revenue is deposited in the Property Tax Replacement Fund. Since the tax credit is effective beginning in tax year 2008 for certified investment made beginning in 2008, and requires IEDC certification, the fiscal impact likely would not begin before FY 2009.

Federal New Markets Tax Credit: The federal New Markets Tax Credit (NMTC) program stimulates economic and community development and job creation in the nation's low-income communities by attracting investment capital from the private sector. Section 45D of the Internal Revenue Code (IRC) allows the federal NMTC for a taxpayer who holds a qualified equity investment in a community development entity (CDE) on the credit allowance date. A qualified equity investment means any equity investment in a qualified CDE if: (1) the investment is a cash investment; (2) substantially used by the CDE to make qualified low-income community investments; and (3) such investment is designated for the purposes of this code section by the CDE. The credit allowance date is the date on which the equity investment in the CDE is initially made, and six anniversary dates each year thereafter. For each of those dates the entity receives a federal tax credit for the equity investment. The credit provided to the investor totals 39% of the cost of the investment and is claimed over a 7-year credit allowance period. In each of the first three years, the investor receives a credit equal to 5% of the total amount paid for the stock or capital interest at the time of purchase. For the final four years, the value of the credit is 6% annually. Investors may not redeem their investments in CDEs prior to the conclusion of the seven-year period.

A qualified CDE is defined as any domestic corporation or partnership with the primary mission of serving, or providing investment capital for, low-income communities or persons. The CDE must maintain accountability to residents of these low-income communities through representation on any governing board of the entity. These CDEs are also required under the IRC to be certified by the Treasury Secretary.

Since 2002, allocations of creditable investment under the NMTC have been awarded by the U.S. Department of Treasury. These allocations represent the amount of investments that were designated as qualifying for the NMTC. The table below reports the creditable investment allocations made to CDEs headquartered in Indiana or national CDEs identifying Indiana as a part of its service area where it would principally focus its activities. In 2006, \$321 M was allocated to three organizations: HEDC New Markets, Inc.; PNC Community Partners, Inc.; and National City New Market Fund, Inc. At the time of this analysis, National City New Market Fund, Inc. had invested \$14 M into Indiana. The remaining two organizations had not invested any portion of their allocation into Indiana.

<u>2007 Allocation</u>: In 2007, \$100 M was allocated to Key Community Development New Markets (KCDNM), headquartered in Cleveland, Ohio serving Indiana among other states nationwide. KCDNM intends to offer subsidized financing for small business loans; and commercial real estate debt and equity for retail centers, single-family housing, industrial developments, small offices, community facilities and mixed-use buildings. With its NMTC allocation, KCDNM will be able to offer interest rates up to 400 basis points below-market, and also offer more flexible credit terms including higher-than-normal-loan-to-value ratios, lower origination fees, longer amortization periods and lower debt service coverage ratios.

	Creditable Investment Allocations for NMTC		
Allocation Year	**Indiana CDEs**	**National CDEs**	**Amount Invested in Indiana**
2002	$6 M	$313 M	n/a
2003-04	$75 M	$15 M	n/a
2005	$0	$140 M	n/a
2006	$0	$321 M	$ 14 M
2007	$0	$100 M	n/a

Explanation of Local Expenditures:

Explanation of Local Revenues:

State Agencies Affected: Department of State Revenue; Indiana Economic Development Corporation; Legislative Services Agency.

Local Agencies Affected:

Information Sources: U.S. Department. of the Treasury, Community Development Financial Institutions Fund, http://www.cdfifund.gov/programs/programs.asp?programID=5#2; Sue Terrell, KCDNM, 216-689-5546; David Trevisani, HEDC New Markets, Inc., 315-525-9234; David Gibson, PNC Community Partners, Inc., 412-762-3081; Michael Taylor, National City New Market Fund, Inc., 216-222-2293.

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